

Minnesota Department of Finance

January 2003

State Revenues on Track in November and December

Net general fund revenues totaled \$2.366 billion during November and December, \$55 million (2.4 percent) more than forecast. Receipts exceeded forecast for each of the major taxes during the past two months, but percentage changes were small. Other tax and non-tax revenues accounted for about two-thirds of the total variance, exceeding forecast by \$37 million.

Summary of Tax Receipts: November – December 2002

	<u>Estimate</u>	<u>Actual</u>	<u>Variance</u>	<u>Percent</u>
	----- (\$ in millions) -----			
Income	886.9	892.6	5.6	0.1
Sales	620.3	634.0	13.7	2.2
Corporate	78.4	77.6	(0.8)	(0.1)
Motor Vehicles	39.8	39.8	0.1	0
Other	<u>685.3</u>	721.8	<u>36.5</u>	<u>5.3</u>
Total	2,310.7	2,365.8	55.1	2.4

Net individual income tax receipts were above forecast by \$6 million, but withholding receipts were \$24 million below projections. Estimated payments and miscellaneous payments made up the difference, leaving a small positive variance. (see page 4) Since fourth quarter estimated payments are not due until January 15, 2003 and more than two thirds of those payments arrive in January, that positive variance could disappear when all payments are in. Lower than anticipated sales tax refunds offset a modest decline in gross sales tax receipts, leaving net sales tax receipts above November's forecast. Deed and mortgage tax receipts were more than \$14 million above projections reflecting continued strong refinancing activity brought on by low mortgage rates. The estate tax, the statewide property tax, the insurance gross premiums tax, and departmental earnings each exceeded forecast levels by at least \$5 million.

Fourth quarter revenue comparisons should always be viewed with caution since variances often reflect timing differences, not changes in the underlying economy. In addition, sales taxes collected by retailers during the December portion of the Christmas shopping season are not remitted until late January. Combined December and January revenue collections will provide a better indicator of how well Minnesota's revenues are tracking November's forecast. That data will be incorporated into the February revenue forecast.

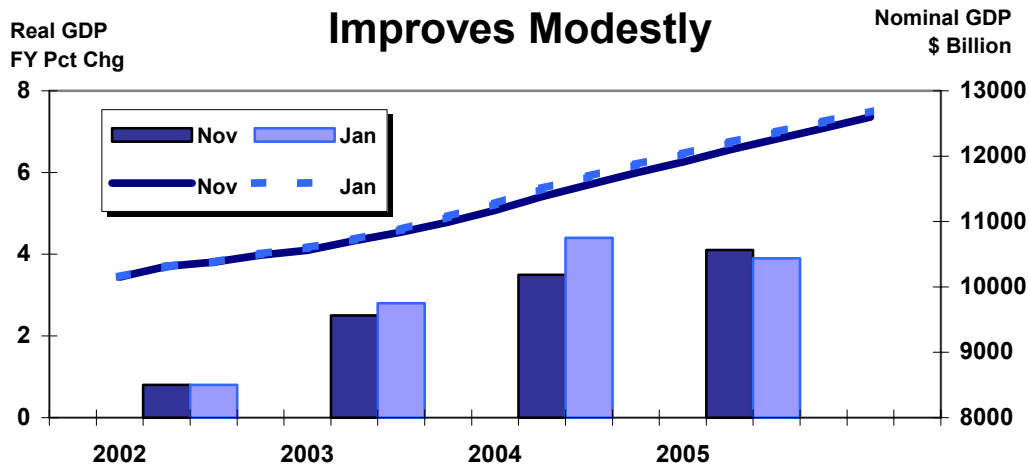
War with Iraq and Federal Stimulus Package Factored into January Baseline Forecast

A stagnant job market, the third consecutive yearly stock market decline, and continued geo-political uncertainty have combined to create the public perception that the U.S. economy is on the ropes, struggling to avoid a double-dip recession. A weak Christmas shopping season, substantial employment declines in November and December, and a widespread belief that the real economic growth rate could have slowed to as low as 1.0 percent in fourth quarter 2002 add to concern about the economy's health.

Most economists, though, expect the economy to continue to grow. Absent an extended war with Iraq only the perennially pessimistic see a recession on the horizon. Even with a sub-par fourth quarter, real GDP growth should average 2.5 percent or more for 2002. That growth rate is well below historical norms for the year following a recession, but the 2001 slump was not deep enough or long enough to create the pent-up demand which usually provides a one-time boost to consumer spending. The Federal Reserve's early rate cuts helped limit the decline. But, that early action led to a more moderate recovery.

The January Baseline forecast from Global Insight, Inc (GII), Minnesota's national economic consultant, calls for real growth to average 2.8 percent in fiscal 2003, followed by growth rates of 4.4 percent in fiscal 2004 and 3.9 percent in fiscal 2005. The Baseline forecast now includes both a short, four-to-six week war in Iraq and a fiscal stimulus package totaling \$50 billion in its first year. In November with neither a war nor a stimulus package in the GII Baseline real growth rates of 2.5 percent, 3.5 percent, and 4.1 percent were projected. Those growth rates, while slower than those of the supercharged years of the late 1990's, are stronger on average than those observed during the 1980's and early 1990's. They also exceed January's Blue Chip consensus outlook.

Economic Outlook for 2004-05 Improves Modestly



Inflation is expected to remain under control through the entire 2004-05 forecast horizon. The CPI is projected to increase 2.4 percent in 2004 and 2.3 percent in 2005. GII assigns a 60 percent probability to its January Baseline forecast, up from November's 55 percent. A more optimistic scenario, which assumes that war with Iraq is avoided, is assigned a

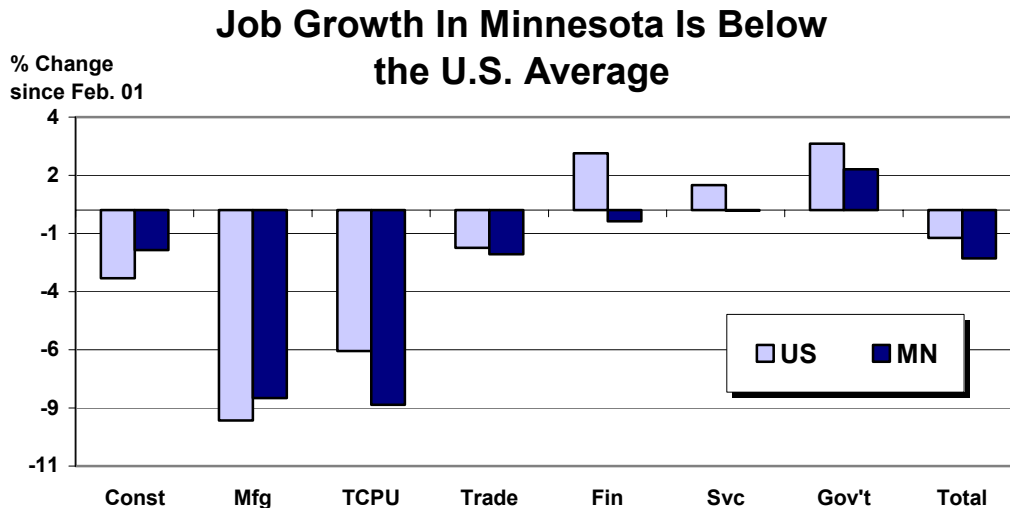
probability of 20 percent, as is a scenario in which the war extends for five months. In the latter scenario real output declines in the second quarter of 2003.

Job Losses in Minnesota Continue to be Greater than the U.S. Average

Payroll employment in Minnesota peaked in February 2001. Then, as the recession started, the number of jobs in the state declined. By December 2001, Minnesota payroll employment had fallen by more than 1.9 percent on a seasonally adjusted basis. State employment recovered slightly during early 2002, stabilizing at a level 1.5 percent below its previous high. Since midsummer though, Minnesota's employment situation has deteriorated. In August, employment fell by about 15,000 jobs, and employment has held at that level through November. Payroll employment in Minnesota is now 2.1 percent below its February 2001 high. Nationally, payroll employment has fallen by just 1.2 percent. Minnesota's November unemployment rate of 3.9 percent, however, remains well below the national rate of 6.0 percent.

The sharp difference between Minnesota and U.S. payroll employment cannot be solely explained by weakness in the manufacturing sector. Manufacturing employment in Minnesota has fallen by 8.1 percent since February 2001. But, that decline is less than the U.S. average of 9.0 percent. And while manufacturing accounts for a greater percentage of total employment in Minnesota than it does nationally, that is not enough to explain the difference.

Other sectors of Minnesota's economy have been hit harder than their national counterparts. Employment in the transportation communications and public utility sector (which includes the airline industry) fell by 6.1 percent nationally, but by 8.4 percent in Minnesota, due in part to the Twin Cities being home to the headquarters of a major air carrier and a regional transportation hub. Employment in wholesale and retail trade also fell slightly faster in Minnesota than elsewhere, and employment in the financial services industry fell in Minnesota while growing nationally. In addition, while employment in the services industry and in government grew in Minnesota, it grew more slowly than the U.S. average.



Comparison of Actual and Estimated Non-Restricted Revenues

(\$ in thousands)

	December Year-to-Date			November & December 2002		
	Forecast Revenues	Actual Revenues	Variance Act-Fcst	Forecast Revenues	Actual Revenues	Variance Act-Fcst
Four Major Revenues:						
Individual Income Tax						
Withholding	2,409,245	2,385,697	-23,548	835,268	811,720	-23,548
Declarations	276,400	295,820	19,420	65,018	84,438	19,420
Miscellaneous	85,000	101,602	16,602	18,861	35,463	16,602
Gross	2,770,645	2,783,119	12,474	919,147	931,621	12,474
Refund	90,000	96,826	6,826	32,232	39,058	6,826
Net	2,680,645	2,686,292	5,647	886,915	892,562	5,647
Corporate & Bank Excise						
Declarations	290,820	287,376	-3,444	126,400	122,956	-3,444
Miscellaneous	67,971	71,007	3,036	17,000	20,035	3,035
Gross	358,791	358,383	-408	143,400	142,992	-408
Refund	99,971	100,379	408	65,000	65,408	408
Net	258,820	258,004	-817	78,400	77,583	-817
Sales Tax						
Gross	1,950,440	1,945,622	-4,817	665,340	660,523	-4,817
Refunds	105,335	86,870	-18,464	45,000	26,536	-18,464
Net	1,845,105	1,858,752	13,647	620,340	633,987	13,647
Motor Vehicle Sales	143,512	143,574	62	39,761	39,823	62
Other Revenues:						
Inherit/Gift/Estate	89,337	95,858	6,521	10,943	17,464	6,521
Liquor/Wine/Beer	32,786	32,051	-735	11,418	10,682	-735
Cigarette & Tobacco/Cont Sub	91,869	92,377	508	28,462	28,970	508
Deed and Mortgage	120,783	135,189	14,407	36,155	50,562	14,407
Insurance Gross Earnings	93,556	98,708	5,153	44,000	49,153	5,153
Lawful Gambling	24,016	24,983	967	8,275	9,242	967
Health Care Surcharge	71,060	69,862	-1,198	24,756	23,557	-1,198
Other Taxes	1,050	1,058	8	136	144	8
State wide Property Tax	261,563	267,175	5,611	260,516	266,127	5,611
DHS RTC Collections	30,020	25,472	-4,547	10,548	6,001	-4,547
Income Tax Reciprocity	49,010	49,010	0	49,010	49,010	0
Investment Income	12,944	14,002	1,058	3,272	4,331	1,058
Tobacco Settlement	148,447	147,568	-879	148,447	147,568	-879
Departmental Earnings	103,333	109,332	5,999	42,898	48,897	5,999
Lottery Revenues	11,979	11,315	-664	4,811	4,148	-664
2001 Sales Tax Rebates	-965	-974	-9	0	-9	-9
Revenues yet to be Allocated	0	1,935	1,935	-2,015	-81	1,934
Residual Revenues Less Refunds	29,676	31,912	2,236	8,209	10,445	2,236
Other Subtotal	1,170,464	1,206,832	36,368	689,843	726,211	36,368
Other Refunds	13,867	13,698	-169	4,546	4,377	-169
Other Net	1,156,597	1,193,134	36,537	685,297	721,834	36,537
Total Gross	6,393,851	6,437,530	43,678	2,457,490	2,501,168	43,678
Total Refunds	309,172	297,774	-11,399	146,778	135,379	-11,399
Total Net	6,084,679	6,139,756	55,077	2,310,712	2,365,789	55,077